11/20/87 RS650-2

JAPAN · ECONOMIC · INSTITUTE

JEI REPORT

NO. 41A October 30, 1987

JAPAN'S FOREIGN AID POLICY: 1987 UPDATE

Summary

In the last year the importance of Japan's economic assistance programs has continued to grow, providing evidence that Tokyo intends to take its "responsibilities as a surplus nation" seriously. Its announcement of several foreign aid initiatives drew worldwide attention, especially its pledge to commit $30 billion in additional funds to the developing countries over a three-year period. Moreover, the appreciation of the yen and a modest real increase in official development assistance disbursements combined to make Tokyo's aid figure skyrocket -- thus bringing Japan back to the number-two donor position. Ironically, though, the new initiatives served to increase cries for Tokyo to do even more to alleviate global debt and development problems. This report will discuss the scope of the new initiatives, the regional aid strategies being proposed, and the significance of the past year for future Japanese aid programs.

Introduction

Japan's official development assistance program is unique in many respects. The economy's rapid growth in the postwar era put Japan in the unusual situation of being a developing and then an ODA donor nation within a very short time. This streamlined economic development was reflected in a succession of rapid changes in Tokyo's ODA program. A 1985 study by aid experts

William L. Brooks and Robert M. Orr* outlined four stages of aid policy. Japan's first foray into aid programs in the mid-1950s took the form of reparations, and although the emphasis shifted after 1965 to foreign aid, the goal remained the same: export promotion -- mainly in Asia -- through tied aid.

It was not until the oil crises of the 1970s that Tokyo began to look beyond Asia to resource-rich developing countries in an attempt to secure the natural resources that are vital to the smooth functioning of the Japanese economy. "Resource diplomacy" was extended to include other political and strategic considerations in the late 1970s when crises in Iran and Afghanistan led Tokyo to further broaden the scope and quality of its aid flows.

Since 1980 Japan has espoused a "basic human needs" approach to aid -- policies to improve the condition of the poor directly rather than to focus on large-scale projects. To do so Tokyo selected four areas of emphasis: rural and agricultural programs; development of new and renewable energy sources; human resource development; and improvement of small- and medium-sized businesses. Inherent in this approach is a commitment to improve the quality of ODA disbursements. Tokyo has also retained its commitment to consider overall security factors when pledging assistance; its policy is to increase aid to those areas that are "important for the maintenance of world peace and stability." It will not, however, extend military assistance to developing countries.

Tokyo's emphasis on basic human needs represents its attempt to deal with another situation that sets Japan's program apart from those of other donors. More than any other government, Tokyo suffers from a perception that its aid program remains largely export-oriented. In response to this problem, Japan has stressed the alleviation of poverty and humanitarian aid -- including emergency and disaster relief -- as well as increased funds for countries with which it has few economic ties, for example, sub-Saharan Africa.

A third factor that contributes to Japan's singularity is its constitutional pledge not to significantly expand its military capabilities. Because this policy restricts the ways it can contribute to international security, Japan has opted to use foreign aid as its primary contribution. Maintaining that economic stability is a necessary prerequisite for political security, Tokyo's assistance has become a major element in discussions of support for the Western alliance. In light of recurring calls from Washington for defense "burdensharing," Tokyo has in a very real sense staked its international credibility as a major power on the effectiveness of its aid program.

Not surprisingly, ODA has become a Japanese bargaining tool not only with developing nations but also with other industrialized countries. Japanese officials are all too sensitive to complaints in this country about its enormous current account surplus as well as the growing perception that the United States rather than Japan has purchased the lion's share of developing-country

*Willim L. Brooks and Robert M. Orr, Jr., "Japan's Foreign Economic Assistance," Asian Survey, XXV, No. 3, (March 1985), p. 323.

The JEI REPORT (ISSN 0744-6489) is published weekly for $40 per year by the Japan Economic Institute of America, 1000 Connecticut Avenue, N.W., Washington, D.C. 20036. Second class postage paid at Washington, D.C. POSTMASTERS: Send address changes to JEI, 1000 Connecticut Avenue, N.W., Washington, D.C. 20036.

manufactured goods, which has exacerbated the U.S. trade deficit. Indeed, Tokyo's oft-used phrase, "Japan's responsibilities as a surplus nation," contains an implicit recognition of the link between U.S.-Japan economic frictions and Tokyo's policies toward the third world. Thus, trade tensions have prompted Tokyo to expand its assistance programs in response to U.S. complaints.

A final unique element of Japan's ODA policy is its emphasis on partnership. Unlike the assistance programs of former colonial powers and the United States, which appear to be more benefactor/recipient oriented, Tokyo stresses "economic cooperation" and "self-help." In the past this translated into higher interest rates and tougher repayment schedules than other donors' loans on the grounds that economic assistance is more effective when obligations and incentives are an integral part of the prgrams. More recently, loans on concessional terms have become more common. Still, the conviction that aid is a partnership is reflected in other ways. For example, officials are reluctant to dictate the types of aid projects that recipients need or to insist on strict oversight activities; rather, they argue that the recipient countries should choose and implement their own development strategies.

Japan's Official Development Assistance in 1986

According to Alan Rix**, Tokyo gives economic assistance to no less than 134 developing countries or territories. Moreover, it has in recent years been the third-largest donor among Organization for Economic Cooperation and Development members after the United States and France (except for a short stint as number-two in 1984). Disbursements soared in 1986 to $5.6 billion -- an increase of 48.4 percent (see Table 1) -- restoring Tokyo to second place (see Table 2). This surge is in sharp contrast to 1985's results, when disbursements fell by 12.1 percent (see JEI Report No. 39A, October 24, 1986).

Much of the change can be attributed to the sharp appreciation of the yen, however. The bulk of Japan's aid is yen-denominated, but the Development Assistance Committee of the OECD calculates ODA in dollar terms. In 1985 the exchange rate averaged Y238.54=$1.00; last year it was Y168.52 -- 41.6 percent higher. Indeed, in yen terms 1986's increase was merely 4.8 percent, with bilateral flows (which are disbursed primarily in yen) rising by 6.3 percent and multilateral flows (largely in dollars) by 1.9 percent. The DAC estimates that in real terms, the increase in Japan's aid amounted to approximately 3 percent, slightly higher than the DAC average.

Other indicators remain below the DAC average, however. Japan's ODA/GNP ratio remained steady at 0.29 percent last year -- significantly below the DAC average of 0.36 (see Table 3) -- holding Tokyo's rank fourteenth of the 18 DAC members. In 1984 its ratio had reached 0.35 percent, close to the average 0.36 percent, but still below the United Nations-recommended level of 0.7 percent.

The quality of aid -- measured by the grant element of ODA -- is another way of evaluating aid programs. Tokyo's ratio of grants to total ODA has consistently been on the low side but it jumped from 73.5 percent in 1985 to 80 percent in 1986. While this is a significant improvement, the grant element is still below the OECD's 86 percent target.

**Alan Rix, Japan's Aid Program (International Development Issues No. 1), Australian Government Publishing Service, 1987.

Table 1: Net Flow of Financial Resources from Japan to Developing Countries and Multilateral Agencies, 1982-86

(in millions of dollars)

Type of Transaction	1982	1983	1984	1985	1986	Percent Change 1985/86
Official Development Assistance	$3,023	$3,761	$4,319	$3,797	$5,634	48.4%
Change Over Previous Year	-4.7%	24.4%	14.8%	-12.1%	48.4%	
ODA/GNP Ratio	0.28%	0.33%	0.34%	0.29%	0.29%	
Bilateral Assistance	2,367	2,425	2,427	2,557	3,846	50.4
Grants	805	993	1,064	1,185	1,703	43.8
Capital Grant Assistance	412	535	543	636	855	34.3
Technical Assistance	393	458	521	549	849	54.7
Development Lending and Capital	1,562	1,432	1,363	1,372	2,143	56.2
Grants, Capital Subscription and Loans to Multilateral Agencies	656	1,336	1,891	1,240	1,788	44.2

Notes: 1. Net disbursement basis.
2. Due to rounding, the figures do not necessarily add up to the totals.

Source: Ministry of Foreign Affairs

Table 2: ODA of Major Donor Countries, 1983-86

(in millions of dollars)

1986 Rank	Country	1983	1984	1985	1986*	Share of Total DAC ODA 1986*
1	United States	$8,081	$8,711	$9,403	$9,784	26.4%
2	Japan	3,761	4,319	3,797	5,634	15.2
3	France**	3,815	3,788	3,995	5,136	13.9
4	West Germany	3,176	2,782	2,942	3,879	10.5
5	United Kingdom	1,610	1,418	1,530	1,750	4.7
6	Netherlands	1,195	1,268	1,136	1,738	4.7
7	Canada	1,429	1,625	1,631	1,700	4.6
DAC Total		27,560	28,686	29,429	37,021	100.0

*Preliminary.
**Including overseas territories and prefectures.

Source: Organization for Economic Cooperation and Development

Table 3: ODA as Percentage of GNP for DAC Countries, 1983-86

(in millions of dollars)

1986 Rank		1983 Amount	1983 Percent of GNP	1984 Amount	1984 Percent of GNP	1985 Amount	1985 Percent of GNP	1986* Amount	1986* Percent of GNP	Percent Change 1985/86*
1	Norway	$584	1.10%	$543	1.02%	$574	1.01%	$796	1.20%	38.7%
2	Netherlands	1,195	0.91	1,268	1.02	1,136	0.91	1,738	1.00	53.0
3	Denmark	395	0.73	449	0.85	440	0.80	695	0.89	58.1
4	Sweden	754	0.84	741	0.80	840	0.86	1,090	0.85	29.8
5	France**	3,815	0.74	3,788	0.77	3,995	0.78	5,136	0.72	28.6
6	Australia	753	0.49	777	0.46	749	0.48	787	0.49	5.1
7	Belgium	480	0.69	433	0.56	440	0.55	542	0.48	23.1
7	Canada	1,429	0.45	1,625	0.50	1,631	0.49	1,700	0.48	4.2
9	Finland	153	0.32	178	0.36	211	0.40	313	0.45	48.3
10	West Germany	3,176	0.48	2,782	0.45	2,942	0.47	3,879	0.43	31.9
11	Italy	834	0.24	1,133	0.33	1,098	0.31	2,423	0.40	120.7
12	United Kingdom	1,610	0.35	1,418	0.33	1,530	0.33	1,750	0.32	14.4
13	Switzerland	320	0.31	286	0.30	302	0.31	429	0.30	41.8
14	Japan	3,761	0.32	4,319	0.35	3,797	0.29	5,634	0.29	-48.4
15	Ireland	n.a.	n.a.	35	0.22	39	0.24	62	0.28	58.8
16	New Zealand	61	0.28	55	0.25	54	0.25	66	0.27	21.0
17	United States	8,081	0.24	8,711	0.24	9,403	0.24	9,784	0.23	4.1
18	Austria	158	0.24	181	0.28	248	0.38	197	0.21	-20.6
DAC Total		27,560	0.35	28,686	0.36	29,429	0.35	37,021	0.36	25.8

*Preliminary.
**Including overseas territories and prefectures.

Source: Organization for Economic Cooperation and Development

Despite these statistics, DAC considers the outlook for Japan's aid program "favorable," primarily because of Tokyo's Third Medium-Term Target, that is, its third aid-doubling plan. The first, announced in 1977, was designed to double the level of that year's disbursements within five years; the goal was met easily as outlays rose from $1.4 billion in 1977 to $3.3 billion in 1980. A second, similar increase was announced for the 1981-85 period. However a slowdown in domestic growth brought fiscal austerity to Japan which -- combined with a sharp depreciation of the yen -- made it impossible to reach the $21.4 billion aggregate goal.

As for the current plan, which was announced in September 1985, Japan has pledged to disburse more than $40 billion in the 1986-92 period as well as to double 1985's $3.8 billion ODA figure in 1992. While the measurable elements of the target reflect the quantity of aid, the plan also stresses improved quality though "effective and efficient implementation." Five goals have been selected with regard to the quality of aid: improved implementation procedures; better coordination between technical assistance and financial allocations; specific evaluation of aid projects; improved coordination with the private sector; and cooperation with other donor countries and international organizations.

In the first half of this year, Tokyo announced that it had narrowed the time frame for the doubling and the $40 billion aggregate goals; it now plans to achieve both by yearend 1990. This decision stemmed from at least two factors. First, some government officials reportedly advocated a shortened time frame in order to take advantage of the strong yen. The sharply inflated dollar value of Japanese disbursements has already brought Tokyo significantly closer to its target. Second, the new target date was announced in conjunction with a domestic stimulus package. Thus, the more ambitious ODA package, along with measures designed to increase Japanese demand, was in part an attempt to quell American criticism of Tokyo's economic policies.

Because of the yen's appreciation, howeve[illegible]bling the 1985 ODA figure in seven years would have required only an approximat[illegible]5.5 percent average annual increase in outlays from now on. The decision earlier this year to shorten the time frame allows the government to take advantage of the strong yen, make the target more ambitious and enhance the visibility of its aid programs all at the same time. In order to disburse some $7.6 billion in 1990, average annual increases of 8 percent will be necessary. This does not appear out of reach, given Tokyo's willingness to expand its aid flows by some 7 percent annually in yen terms and the fact that the exchange rate could easily jump higher than 1986's average -- at least in the foreseeable future.

Still, although the 1985 aid-doubling goal is virtually assured, it is not certain whether Tokyo will disburse the $40 billion total also outlined in the Third Medium-Term Target. Even if Japan disburses $7.6 billion in 1990 (assuming a 8 percent annual growth), the total for the 1986-90 period will only add up to about $33 billion using 1986's exchange rate. Conversely, if Tokyo retains its 7 percent annual increase in ODA outlays, an average exchange rate of Y135.7 would be needed to reach the $40 billion mark.

Recycling the Surplus for LDC Development

Even more important than the revisions to the doubling plan was Japan's decision to pump some $30 billion into the developing countries over a three-

year period. Announced by Prime Minister Yasuhiro Nakasone earlier this year, the plan consists of roughly $10 billion that had been previously pledged to multilateral lending institutions, and another $20 billion designed to recycle a portion of Japan's current account surplus directly to the developing countries. A more detailed breakdown follows.

$10 Billion to Multilateral Development Institutions

$2.6 billion - FY 1988-1990 subscriptions to the International Development Agency (the low-interest arm of the World Bank).

$3.6 billion - (3 billion in Special Drawing Rights) for the International Monetary Fund as a special facility to deal with unusually critical situations that require "financial support beyond the usual recourse."

$2.0 billion - Special fund for the World Bank: $200 million in grant money from Japan and $1.8 billion to be raised by the World Bank in the Tokyo capital market.

$1.3 billion - Funds for the Asian Development Foundation (a window of the Asian Development Bank).

$9.5 billion - Total

$20 Billion Recycling Initiative

$8.0 billion - Further government contributions to multilateral lending agencies, including the World Bank, the Inter-American Development Bank, the Asian Development Bank and the African Development Bank.

$9.0 billion - Untied loans by the Overseas Economic Cooperation Fund, the Export-Import Bank of Japan and possibly private banks co-financed by the World Bank. (Projects are to be chosen in consultation with the World Bank and will follow the strict lending standards of the Bank.)

$3.0 billion - Export-Import Bank untied loans.

$20 billion - Total.

The recycling program is primarily a response to debt rather than development problems. While particularly aimed at the Latin American countries, officials have stressed that debtor nations in other parts of the world will receive funds as well. Recipients will probably be middle-income developing countries, say officials, since ODA is more appropriate for poorer LDCs and LLDCs (least developed countries). Nonetheless, some of the recycling monies are certain to qualify as official development assistance according to DAC criteria. One Japanese official indicated that he would like to see between one-fourth and one-third of the $20 billion qualify as ODA.

What may be more significant about the recycling plan is the precedent that it sets for Japanese aid policy. In the past Tokyo has stressed that the private sector should be wholly responsible for finding a solution to the debt crisis, and has emphasized the importance of new private loans and increased direct investment. However, the existence of a plan that outlines several possible governmental responses to the debt problem suggests that Tokyo may be considering the need to expand the scope of its assistance programs to include debt as well as development issues. If this is the case, the endorsement of Treasury Secretary James Baker's emphasis on a private-sector solution to the debt crisis may give way to a recognition of the need for government involvement -- or, at the very least, increased government private-sector cooperation.

Japanese officials have already called for more multilateral initiatives to promote debt-to-equity swaps, provide risk insurance and develop other responses to the problem. No major new steps will be taken at the national level, they say, until Tokyo can assess the effectiveness of the recycling policy. Still, the innovativeness of the recycling plan may portend more to come. (For a discussion of Japan's response to the Latin American debt crisis, see JEI Report No. 29A, July 31, 1987.)

Taking the Lead in Multilateral Initiatives: MIGA

Tokyo again seized the initiative in June, becoming the first industrialized country to ratify the convention establishing the Multilateral Investment Guarantee Agency. Thirteen developing nations have already ratified the convention, while 45 other countries (including the United States) have signed but not officially adopted the document. Although Japan had initially intended to follow Washington's lead, it reversed its decision -- partly in preparation for last June's economic summit in Venice and partly because of mounting uncertainty as to whether the United States would ratify the convention.

As proposed, MIGA would consist of members of the World Bank and Switzerland and would issue guarantees against non-commercial risks to participants willing to invest in a member developing nation. These include (1) losses due to currency transfers; (2) losses incurred by expropriation or similar actions; (3) losses associated with a breach of contract; and (4) losses stemming from war and civil disturbance. MIGA would also guarantee other types of non-commercial risks if specifically requested by the investor and the host country (see JEI Report No. 22B, June 12, 1987).

A Changing Global Outlook?

Japan has always given the bulk of its ODA to Asia, stressing its historic, political and economic ties with the region as well as its responsibility to contribute to the economic stability of the continent. In fact, by the end of the 1970s a 7-1-1-1 formula was institutionalized: approximately 70 percent of total disbursements went to Asia, while Africa, Latin America and the Middle East received roughly 10 percent apiece. While this ratio has begun to change in recent years, Asia will hold the number-one position -- by a long shot -- for the foreseeable future. In 1986 it received some 65 percent of total disbursements (see Table 4); moreover, Asian countries accounted for nine of Japan's top ten aid recipients (see Table 5).

Table 4: Japan's Bilateral ODA by Region, 1981-86

(in millions of dollars)

Year	Total	Asia	Middle East	Africa	Latin America	Europe	Oceania	Unallocable
1981	$2,260 (100.0%)	$1,605 (71.0%)	$190 (8.4%)	$211 (9.3%)	$177 (7.8%)	$-2 (-0.1%)	$19 (0.9%)	$62 (2.7%)
1982	$2,367 (100.0%)	$1,624 (68.6%)	$194 (8.2%)	$268 (11.3%)	$184 (7.8%)	$-3 (-0.1%)	$23 (1.0%)	$77 (3.2%)
1983	$2,425 (100.0%)	$1,614 (66.5%)	$150 (6.2%)	$287 (11.8%)	$241 (9.9%)	$23 (1.0%)	$18 (0.7%)	$93 (3.8%)
1984	$2,427 (100.0%)	$1,594 (65.7%)	$249 (10.3%)	$211 (8.7%)	$229 (9.4%)	$1 (0.0%)	$25 (1.0%)	$117 (4.8%)
1985	$2,557 (100.0%)	$1,732 (67.8%)	$201 (7.9%)	$252 (9.9%)	$225 (8.8%)	$1 (0.0%)	$24 (0.9%)	$122 (4.8%)
1986	$3,846 (100.0%)	$2,494 (64.8%)	$340 (8.8%)	$418 (10.9%)	$317 (8.2%)	$2 (0.1%)	$55 (1.4%)	$221 (5.7%)

Note: Net disbursement basis.

Source: Ministry of Foreign Affairs

Table 5: Major Recipients of Japan's ODA, 1982-86

(in millions of dollars)

1982		1983		1984		1985		1986	
Country	Amount	Country	Amount	Country	Amount	Country	Amount	Country	Amount
China	$369	China	$350	China	$389	China	$388	China	$497
Indonesia	295	Thailand	248	Malaysia	245	Thailand	264	Philippines	438
Bangladesh	216	Indonesia	236	Thailand	232	Philippines	240	Thailand	260
Thailand	170	Philippines	147	Indonesia	168	Indonesia	161	Bangladesh	248
Philippines	137	India	130	Philippines	160	Burma	154	Burma	244
Burma	104	Burma	114	Bangladesh	123	Malaysia	126	India	227
Pakistan	95	Bangladesh	104	Burma	95	Bangladesh	121	Indonesia	161
Malaysia	75	Malaysia	92	Egypt	81	Pakistan	93	Pakistan	152
Sri Lanka	62	Sri Lanka	73	Pakistan	67	Sri Lanka	84	Sri Lanka	127
Egypt	62	Pakistan	73	Sri Lanka	64	Egypt	73	Egypt	126

Note: Net disbursement basis.

Source: Ministry of Foreign Affairs

Until recently, however, there appeared to be only sketchy policies regarding other regions, except that each would receive about 10 percent of Japan's annual foreign aid. With the announcement of the recycling plan, Japan has begun to outline specific differences in its regional aid policies.

Asia - The major recipients of Japanese aid in Asia are the People's Republic of China, members of the Association of Southeast Asian Nations and Burma. This region is important enough to Japan to warrant a discussion of three sub-regions:

Northeast Asia - Almost all of Tokyo's aid to Northeast Asia goes to the PRC. China has displaced ASEAN members as the top recipient -- with almost 13 percent of Japan's bilateral disbursements -- and has held that position since 1982. China has reportedly been promised at least $700 million of the $20 billion in recycling funds. South Korea also used to be a major recipient of Japanese aid. Today, however, although a fair percent of Japanese money is in Korea, little of it qualifies as ODA. In 1986, for example, Korea's total ODA from Japan was negative -- meaning that loan repayments exceeded the amount of new loans and grants.

Southeast Asia - ASEAN members (Thailand, Indonesia, Singapore, the Philippines, Malaysia and Brunei) were heartened by Foreign Minister Tadashi Kuranari's pledge of a $2 billion "ASEAN Fund" last June. According to Prime Minister Nakasone, the fund will be used to stimulate the "growth of the private industrial sector, including joint ventures, and [to] contribute to the future development of financial markets in the ASEAN area (see JEI Report No. 39B, October 10, 1987, and JEI Report No. 14A, April 10, 1987).

ASEAN countries received some 24 percent of total bilateral flows in 1986, a drop from 1985. Still, this group of nations is given top priority in Tokyo's aid program; Japan rarely makes a significant ODA decision without considering possible ASEAN reactions.

Southwest Asia - This region has traditionally received the smallest share of Japan's aid to Asia, but its ratio jumped from 15 percent of total bilateral flows in 1985 to almost 22 percent in 1986. Four of Tokyo's top 10 recipients are South Asian countries, and during a recent visit, Mr. Kuranari indicated that Japan would lend India an additional Y68.5 billion ($489.3 billion at Y140=$1.00) -- the largest amount Japan has ever lent to that country.

Latin America - Debt problems here prompted the recycling initiative, but ODA is a different story. Latin America received only 8 percent of total bilateral disbursements in 1986 -- partly because the high per-capita income of several Latin American countries makes them ineligible for aid. It appears likely, however, that Japan will increase its activities in Latin America through increased incentives for private initiatives and expanded government/private-sector cooperation in financing loans.

Africa - Africa receives the second-largest share of Japanese aid, about 11 percent of total bilateral flows. The sub-Saharan region is likely to remain in the second slot, both because of its dire needs and because there is still considerable room for expansion. Tokyo tends to stress this area when discussing its humanitarian aid initiatives. Not only does the basic human needs approach apply but since Japan has fewer cultural, political and economic

links to this region than any other area in the world, expanded aid is the most obvious way to display an absence of ulterior economic motives.

Few, if any, of the recycling funds are likely to wind up in Africa, largely because most African debt is owed to governments rather than to banks and conventional assistance may be more effective for the region. Consequently, Japan recently promised an additional $500 million in grant aid for sub-Saharan Africa and other LLDCs. Kyodo News Service reports that Kenya may be the first country to receive this aid; Zambia and the Sudan have also expressed an interest.

Middle East - This is the only region for which Japan has not outlined an assistance strategy during the last year. Like Latin America, many per-capita incomes here are too high for ODA eligibility. With regard to aid considerations, though, Foreign Ministry officials point out that the region's oil supplies do influence Tokyo's policy.

In addition to resource concerns, "comprehensive national security" considerations are also noticeable in the Middle East. First embraced by then-Prime Minister Masayoshi Ohira in 1980, comprehensive national security involves both military and non-military factors. This linking of defense, energy and other economic needs has led to an increase in ODA for those countries (in the Middle East and elsewhere) that are important to the Western alliance. Egypt, for example, is one of Tokyo's top ten aid recipients. Moreover, Tokyo has reportedly also approved a Y54.4 billion ($388.6 million) Ex-Im Bank/World Bank co-financed loan for Turkey under its recycling plan.

Criticisms

Two of the most controversial aspects of Tokyo's aid program concern mixed credits and tied aid. American critics have long charged that Japan and European nations mix foreign aid with export credits on commercial terms to win contracts in developing countries. Tokyo stresses that it shares this country's desire to minimize the use of mixed credits and, as a result, joined other OECD members earlier this year in a move to tighten the rules governing project financing (see JEI Report No. 10B, March 13, 1987, and No. 12B, March 27, 1987).

While the fight over mixed credits has ended -- at least for now, critics continue to charge that the informal procedures involved with Japanese programs limit project participation to Japanese businesses.*** For example, Tokyo employs a "request only" policy, meaning that development proposals cannot originate in these government agencies that are involved in the aid program. While this is based on the premise that the objectives of the recipients should be respected, it also allows Japanese companies to lobby recipient governments to request specific projects. Moreover, the requirements for official feasibility studies before a project is approved encourage the participation of Japanese consultants at an early stage in the process, paving the way for later Japanese contracts.

***On paper, Japan's record looks good. OECD figures show that Japan's use of tied aid is lower than that of the United States.

The request-only procedure has at least one other unfavorable consequence, according to recipient-nation observers. Since developing-country elites are in a position to issue requests, projects are often capital-intensive rather than directly oriented to the needs of the poor. In view of these complaints Tokyo has taken steps to correct the situation by sending study missions to developing countries to determine assistance needs and suggest possible aid projects.

Another obstacle is the fact that ODA decisions often require the consensus of four ministries whose interests and priorities differ: Foreign Affairs, Finance, International Trade and Industry, and the Economic Planning Agency. These bureaucratic stumbling blocks are only intensified by the fact that several other agencies are also involved in specific aspects of ODA programs (see Table 6).

Table 6: Japan's Aid Expenditures by Ministry, FY 1985-FY 1986

(in billions of yen)

Ministry or Office	FY 1985 (Revised)	FY 1986 (Initial)	Percent Change
Office of the Prime Minister			
Grants to Overseas Economic Cooperation Fund	Y29.5	Y31.8	7.8%
Ministry of Foreign Affairs	286.0	305.9	7.0
Economic development assistance	115.0	124.0	7.8
Grants to Japan International Cooperation Agency	83.6	90.9	8.7
Subscription to Japan International Cooperation Agency	4.3	4.9	14.0
Contributions to international aid programs*	81.1	84.1	3.7
Ministry of Finance	232.5	250.0	7.5
Subscription to Overseas Economic Cooperation Fund	169.0	180.0	6.5
Food production projects	59.4	61.0	2.7
Subscription to multilateral development banks	4.1	9.1	123.0
Ministry of Education			
Allowance for government-sponsored students in Japan	6.7	7.9	17.9
Ministry of Health and Welfare			
Contributions to World Health Organization	6.2	5.8	-6.5
Ministry of Agriculture, Forestry and Fisheries			
Promotion of international fisheries cooperation	4.3	4.4	2.3

Ministry of International Trade and Industry	16.1	17.5	8.7
Overseas development planning research	6.6	7.1	7.6
Foreign technician training projects	3.7	4.1	10.8
Dispatch of private experts	4.7	5.2	10.6
Total	581.2	623.2	7.2
*Contributions to international aid programs	81.1	84.1	3.7
United Nations	16.1	15.6	-3.1
U.N. Food and Agriculture Organization	4.2	5.2	23.8
UNESCO	1.7	3.8	123.5
Organization for Economic Cooperation and Development	2.6	3.0	15.4
U.N. Development Program	13.5	14.2	5.2
World Reserve Food Program	2.7	3.1	14.8
U.N. Children's Fund (UNICEF)	3.0	3.3	10.0
U.N. High Commissioner's Refugee Program	11.5	11.0	-4.3
U.N. Population Activity Fund	9.0	9.6	6.7
Middle East Refugee Help Program	2.0	2.0	0.0
International Agricultural Study Conference Group	2.8	3.1	10.7
Other	12.1	10.2	-15.7

Source: Ministry of Finance, Financial Statistics of Japan, Fiscal Year 1986

An Expanded Role For Japan?

Although Japan's recycling initiative and revised doubling plan have been warmly welcomed in developing and industrialized countries, there has already been some grumbling about the program's scope. In short, observers say, Tokyo is in a position to do even more. According to Washington Post columnist Hobart Rowen, for example, the recycling plan is "not enough but at least a start." Moreover, the Economist points out that $10 billion of the $30 billion total was already pledged before the announcement of the package and that the $2 billion special fund for the World Bank amounts to nothing more than encouraging the organization to raise more money in Japan's capital market.

There have been specific proposals outlining a greater role for Japan in international development. A highly publicized one comes from the World Institute for Development Economics Research, headed by former foreign minister Saburo Okita. The organization suggests that Japan recognize that it will run a substantial current account surplus for the next several years and rather than trying to eliminate the surplus, should send more excess funds to the developing countries. WIDER has suggested channeling $25 billion annually to the LDCs over a five-year period and tripling the 1985 ODA figure by 1990 (see JEI Report No. 35B, September 18, 1987).

Another proposal, this one originating with American observers, calls for a Japanese "Marshall Plan" on the order of American efforts in postwar Europe. Japanese spokesmen say that would be difficult since Japan's surplus

funds are in the private sector. The government, by contrast, continues to run a sizable budget deficit. For this reason Tokyo has made private-sector participation an integral element of the recycling initiative.

The U.S. Senate, too, has jumped on the proposal bandwagon. In September it added an amendment to S 1174, the Defense Department authorization bill, calling on Japan to increase its ODA disbursements to 3 percent of GNP by 1992 (see JEI Report No. 37B, October 2, 1987). In light of Japan's current 0.29 percent level, this target is unlikely. Finance Minister Kiichi Miyazawa reportedly expressed anger about the amendment, especially in light of Tokyo's present efforts to expand assistance via its $30 billion plan.

Yet another suggestion is that Japan should contribute more to the political leadership of the multilateral institutions, especially the World Bank. According to the Far Eastern Economic Review, for example, "Japan is in the best position to fill much of the vacuum caused by the lack of U.S. intellectual leadership in the World Bank." This may be a viable option, although no moves have been announced as yet. To date Japan has been content to expand its financial contributions and follow Washington's political leadership.

Given Tokyo's preference for aid to promote international stability, it is not unlikely that there will be a continuing search for creative government/private-sector cooperation on debt and development problems. With regard to financial commitments, however, officials intend to wait until they can assess the success of the $30 billion plan before pledging any major new funds.

Conclusion

MITI's 1986 White Paper on Economic Cooperation cites four structural problems in Japan's aid efforts. First, the debt problem constitutes an obvious impediment to development goals. Second, the low level of primary commodity prices reduces the foreign exchange earnings of developing countries and restricts their economic growth. Third, trade protectionism could inhibit economic growth in the LDCs since the expansion of world trade is an "important precondition of economic and social development." And fourth, problems of food and agricultural development in the LDCs impede the attainment of other development goals.

These problems notwithstanding, 1986-87 may represent a landmark for Japan's assistance program. The decision to embrace new aid programs (including those that respond to debt problems) and as take the lead on issues such as MIGA may indicate the beginning of a more expansive role for Japan. At the very least these initiatives provide sound evidence of Tokyo's intention to take the "responsibilities of a surplus nation" seriously.

For further information contact Eileen Marie Doherty.

* * * * * *

The views expressed in this report are those of the author and do not necessarily represent those of the Japan Economic Institute.

Appendix: Distribution of Japan's Bilateral ODA Commitments, 1985-86*

(in millions of dollars)

	1985	1986	Percent Change 1985/86	Percent of Total 1985	Percent of Total 1986
Public utilities	$1,756.6	$1,510.8	-14.0%	43.1%	34.8%
Planning and public administration	25.8	30.8	19.4	0.6	0.7
Agriculture and fisheries	699.5	521.9	-25.5	17.2	12.0
Industry, mining and construction	432.1	530.5	22.8	10.6	12.2
Trade, banking, tourism and services	18.7	30.7	64.2	0.5	0.7
Education	317.8	362.6	14.1	7.8	8.4
Health	161.9	135.5	-16.3	4.0	3.1
Social infrastructure and welfare	117.7	158.1	34.3	2.9	3.6
Multisector	98.6	23.7	-76.0	2.4	0.5
Unspecified**	144.6	245.4	69.7	3.6	5.7
Not allocable by sector***	302.4	792.0	161.9	7.4	18.2
Total	4,075.6	4,341.9	6.5	100.0	100.0

*Commitment basis

**Includes administrative costs.

***Includes commodity loans, food aid, debt relief and other types of aid.

NOTE

ONLY THE FOLLOWING PAGES OF THIS

PUBLICATION HAVE BEEN FILMED

Pages: 1-4, 7, 8